Supreme Court, U.S.
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No. 91-1269

IN THE

**SUPREME COURT OF THE UNITED STATES**

OCTOBER TERM, 1991

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U. S. METROLINE SERVICES, INC.

*Petitioner,*

*v.*

SOUTHWESTERN BELL TELEPHONE COMPANY,

*Respondent.*

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# PETITIONER'S REPLY BRIEF

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## REPLY AND OBJECTIONS TO RESPONDENT'S STATEMENT OF THE CASE[1]

At pages 4, 5 and 6 of its Statement and, later, at pages 13, 14, 25 and 26 of its Brief, Respondent persistently makes statements outside the Record, and irrelevant to an appeal of a dismissal of Petitioner's Complaint under Rule 12(b)(6). Respondent's allusions to an "audit"; to Petitioner "reselling" local telephone service; to the operation of a radio common carrier service by an unrelated, earlier company; to what Respondent "believed" about that other company [pp. 4,5 & 6]; to "no new technology issues" [pp. 13, 14]; and to Respondent's various tariffs and a PUC adjudicatory hearing on tariff issues — none of this has any bearing on Petitioner's suit in the lower court for antitrust violations and damages. Moreover, none of those extraneous subjects have anything to do with the errors of law committed by the courts below.

## SUMMARY OF ARGUMENT

The District Court and the Circuit Court made egregious errors in using the state action doctrine to grant and affirm Respondent Southwestern Bell's Rule 12(b)(6) motion to dismiss the antitrust causes of action well-stated in Petitioner's Amended Complaint.

First, both courts entirely ignored the proper standards in rulings on Rule 12(b)(6) motions to dismiss, established by this Court in *Conley v. Gibson*, 351 U.S. 41, 78 S.Ct. 99 (1957).

Second, to excuse the application of proper *Conley* standards, both courts erroneously used the "law of the case" to justify a dismissal of Petitioner's Complaint, when that doctrine does not bridge the gap between a preliminary injunction proceeding and a subsequent disposal of the main case on the merits.

Thirdly, just as the courts below ignored fundamental procedural standards in wrongly dismissing Petitioner's Complaint, they declined to make a serious analysis — or really

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[1] Please see Appendix of Petitioner, Section I, for the listing of parent companies and subsidiaries of Southwestern Bell pursuant to Rule 29.1.

any analysis — of the statute at issue, the Texas PURA. Rather, the courts below misidentified the *challenged conduct* of Respondent: the arbitrary threat to cut off the telephone lines of Petitioner, a competitor in the competitive market of metro line service. Inexplicably, the courts below decided Petitioner was challenging the Respondent's *rate* tariffs, when there is no remote suggestion of such a claim by Petitioner anywhere in its Amended Complaint.

From that entirely erroneous premise, the courts below applied, without analysis, the *Parker v. Brown* state action doctrine, effectively *immunizing* Southwestern Bell Telephone Company from the duty of responsible conduct under the federal antitrust laws.

The Respondent's arguments are clumsy and misguided efforts to bolster the courts below, by grossly misapplying the *Midcal* test and by concocting purportedly "factual" statements from outside the record. Indeed, Respondent seems not to understand either (1) that this case is an appeal of the Rule 12(b)(6) judgment of dismissal of Petitioner's Amended Complaint and, accordingly, (other than the text of the Amended Complaint itself, R -18) the Record is not an issue at all; or (2) that it is the articulation of policy of the State, *by* the State, and the active supervision of that policy of the State, *by* the State, as found in the *PURA itself*, which is the proper object of the *Midcal* two-pronged analysis. Respondent apparently thinks that *Midcal* is to be applied to Respondent's *own* "enforcement of rates" which Respondent characterizes as the *policy* of the State. The Respondent's conduct is the challenged conduct, not State policy.

Respondent's confusion and misstatements about Rule 12(b)(6) law, the identification of the correct subject of analysis and the purpose of a *Midcal* analysis permeate Respondent's Brief in Opposition.

In this Reply, Petitioner hopes to clarify the confusions presented by Respondent in its attempt to excuse the multiple errors made by the lower courts in a straightforward antitrust damages case.

## ARGUMENT

### 1. Respondent is not immune from antitrust liability under the state action doctrine.

Respondent's arguments regarding the applicability of the two-pronged *Midcal* test to the Texas PURA are misplaced and singularly unpersuasive. Instead of dealing with the specific *anticompetitive conduct alleged in the Complaint*, Respondent argues about the "rate-making" features of the PURA — features which are not relevant to this lawsuit. Respondent makes the ludicrous claim that Southwestern Bell's "obligation to enforce its tariffs as they apply to Petitioner or any other similarly situated customer and to charge the appropriate tariffed rate for a service is clearly articulated and affirmatively expressed as state policy, (PURA sections 2, 46) ..." [Respondent's Brief at p.14-15]. The argument is both irrelevant and wrong.

A. In attempting to apply the first prong of the *Midcal* test, Respondent's brief (pp. 12-21) betrays a seriously confused application of *Midcal*.

First, Respondent apparently thinks that the "challenged conduct" of Respondent is its "enforcement" of its rate tariffs. Petitioner's Amended Complaint does *not* remotely address or challenge Respondent's rates; or how rates were set; or whether some rates are high and others low; or whether any rates of Respondent are or are not reasonable or lawful. Those are matters for a regulatory agency, the Texas PUC.

Here, Petitioner's Amended Complaint (R.18) challenges very specific conduct of Respondent: threatening to cut off Petitioner's telephone lines. That is the "challenged conduct" which is to be addressed in applying the *Midcal* test. Because Respondent's red herring — its claimed enforcement of its own rate tariffs — was the *excuse* Respondent gave in its *brief* to the trial court (R.21), that does not alter the allegations in Petitioner's Amended Complaint. And it is *only the allegations in Petitioner's Amended Complaint* which are to be reviewed in ruling on a Rule 12(b)(6) motion to dismiss that complaint.

Secondly, it is not Respondent's conduct in "enforcing its rate tariffs" which is the proper subject of a *Midcal* analysis of a "clearly articulated state policy"; rather, the application of the first prong of the *Midcal* test required the courts below to analyze the Texas *statute* — the PURA. The courts below should have reviewed that statute to determine if *it* represented a clearly articulated policy of the state to permit Respondent's challenged conduct: threatening to cut off the telephone lines of a competitor.

Respondent wrongly relies on *Southern Motor Carriers Rate Conference v. United States*, 105 S.Ct. 1721 (1985), for the proposition that Texas intended to displace competition with a "permissive" regulatory structure. The Court in *Southern* was dealing with what was, on its face, "an anticompetitive regulatory system" which, by state statute, permitted large "rate bureaus" of motor carriers to collectively engage in overt price fixing agreements. Moreover, in discussing *Midcal*, the Court in *Southern* stated that the first prong of the *Midcal* test is satisfied: "*As long as the state as sovereign clearly intends to displace competition in a particular field with a regulatory structure* . . . ." *Id.*, 105 S.Ct. at 1731 (emphasis added). There is literally nothing in PURA or its construction by the Texas courts suggesting any intention of Texas to "displace competition" in the field of telecommunications in general, or in the competitive metro services market in particular.

B. With regard to the second prong of *Midcal*, Respondent must show that the State of Texas exercises "ultimate control over challenged competitive conduct" and that the "state officials have and exercise power to review *particular anticompetitive acts* of private parties *and disapprove those* that fail to accord with state policy." *California Retail Dealer's Assn. v. Midcal Aluminum, Inc.*, 445 U.S. 97, 100 S.Ct. 937 (1980); *Patrick v. Burget*, 486 U.S. 94, 101 (1988).

Respondent claims that the case before this Court should be distinguished from *Cantor v. Detroit Edison Co.*, 428 U.S. 579, 96 S.Ct. 3110 (1976), because the commission in this case has the

power to approve tariffs. But, so did the Michigan Commission; the distinction is a false one. Also, the mere power to approve tariffs is insufficient to meet *Midcal's* active supervision requirement. In *Cantor*, this Court held that:

> We concluded that neither Michigan's approval of the tariff filed by respondent, nor the fact that the lamp exchange program may not be terminated until a new tariff is filed, is a sufficient basis for implying an exemption from the federal antitrust laws for that program." *Id.*, 428 U.S. at 599, 96 S.Ct. at 3121.

Respondent erroneously asserts that "*Southern Motor Carriers* expressly rejected certain premises of *Cantor* referring to the *Cantor* language setting forth the 'necessity' requirement as 'questionable dictum'". (Respondent's Brief, p. 27) That is not correct. Footnote 21 in the *Southern Motor Carriers* opinion, 105 S. Ct. at 727, is only a rejection by the majority of an argument by the *dissent* to the effect that state regulatory programs are entitled to antitrust immunity only if an antitrust exemption is necessary to make the program work. In the same paragraph of the text of that opinion, however, the court *confirms* the second prong of its test in *Midcal* by stating: "Second, the state must supervise actively any private anticompetitive conduct ... This supervision requirement prevents the state from frustrating the national policy in favor of competition by casting a 'gauzy cloak of state involvement' over what is essentially private anticompetitive conduct." *Id.*, 105 S.Ct. at 1727. Clearly, this Court in both *Southern Motor Carriers* and *Cantor* was emphasizing the standard that officials of the State of Texas must actively supervise Bell's "private anticompetitive conduct".

Likewise, there is no merit to Respondent Bell's claim that *Southern Motor Carriers'* alleged "limitation of *Cantor*" is found in *Benton* (Respondent's Brief, p. 27). First, in *Benton, Benton and Benton v. Louisiana Public Facilities Authority*, 897 F.2d 198 (5th Cir. 1990), the Circuit Court was dealing with a suit by a law firm directly *against a public agency*, the Louisiana Public Facilities Authority, for conspiracy with others to monopolize the business of providing bond counsel services by bonds issued on

that public agency. The Circuit Court properly concluded that, because the Louisiana Public Facilities Authority is a state agency, the second prong of *Midcal*, active state supervision, is not required under this Court's decision in *Hallie v. Eau Claire*, 471 U.S. 34 (1985).

Further, this Court in *Cantor* was not dealing with a state agency, but rather with a *private party*, just as the courts here are dealing with the conduct of Respondent Bell. In fact, the Fifth Circuit, in *Benton*, described the *Cantor* decision as a holding by the this Court that "*... mere approval by a state ratemaking commission of a private utilities tariff which violated the Sherman Act was not compelled state activity beyond the reach of the Sherman Act.*" *Id.*, 897 F.2d at 204 (emphasis added). Thus, the Fifth Circuit has made it clear that a "public" utility is a "private party". *Benton* makes a clear distinction between a public agency and private parties, for the application of the second prong of *Midcal*. When the defendant is a private party, as here, both prongs of the *Midcal* test must be applied. Defendant Bell is a private company, which, due to its monopoly power in some markets, is a public utility subject to rate regulation by the Texas PUC in those markets. PURA Secs. 2 and 3 (c) (2) (A), (B), the latter section defining public utility in the communications field as a "dominant carrier" which has sufficient *market power* in *a* telecommunications market ... to enable such provider to control prices in a manner adverse to the public interest ..." (emphasis added).

Consistent with this Court's *Cantor* decision, a public utility cannot claim antitrust immunity merely because its tariff either has been filed with or approved by a state ratemaking commission. The Fifth Circuit's 1990 opinion in *Benton*, therefore, confirms a principle argument of Petitioner.

2. **In its per curiam opinion in the first appeal, the Fifth Circuit did not hold that Respondent Bell is immune from antitrust liability under the state action doctrine; and the Court wrongfully applied the law of the case to the Rule 12(b)(6) dismissal.**

At pages 8-12 of the Respondent's Brief, Respondent Bell heavily relies upon a footnote in the Circuit Court's *per curiam* order in the first appeal dealing with injunctive relief, *DFW Metro Line Services v. Southwestern Bell*, 901 F.2d 1267 (5th Cir. 1990), *cert. denied*, 111 S. Ct. 519 (1990). However, the only *holding* of the Fifth Circuit was that Petitioner had not proved the requisite element of irreparable injury (which was the subject of the bulk of the oral argument before the Panel on April 3, 1990). The Respondent argues that footnote 6 of the Court's *per curiam* opinion became the "law of the case". Whether as an afterthought, a comment or otherwise — but clearly only dictum — footnote 6 of the Circuit Court's *per curiam* opinion did not become the "law of the case".

This appeal is, in part, from the Circuit Court's erroneous use of the "law of the case" in the injunction proceeding to affirm the trial court's later Rule 12(b)(6) dismissal of Petitioner's antitrust damage suit. Granting and affirming the motion to dismiss means that both courts below necessarily ruled, as a matter of law, that "... it appears beyond doubt that the Plaintiff can prove no set of facts in support of his claim which would entitle him to relief". *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957).

Contrary to Respondent's assertions, *Milgard Tempering, Inc. v. Selas Corp. of America*, 902 F.2d 703 (9th Cir. 1990), supports Petitioner's position. The *Milgard* court had held in a prior appeal of the case that: "Pursuant to Section 28.1(f) of the purchase contract in Wash. Rev. Code, 4.84.330, [Selas] being the prevailing party herein, is entitled to reasonable attorneys' fees and costs." *Id.*, 902 F.2d at 715. In the subsequent appeal, the Ninth Circuit determined that this language about the "prevailing party" was dicta and therefore not the "law of the case".

The same principle applies to the case here. Footnote 6 was not necessary to the result reached in the *per curiam* opinion of the Fifth Circuit. Therefore, it should not be the law of the case in the second appeal. That is because the law of the case doctrine gives no preclusive effect to *dicta*. *Ducey v. U.S.*, 830 F.2d 1071 (9th Cir. 1987).

Likewise, *Kennedy v. City of Cleveland*, 797 F.2d 297 (6th Cir. 1986), *cert. denied*, 479 U.S. 103 (1987), supports Petitioner's argument that it is error to apply a holding in an earlier preliminary *injunction* proceeding as the law of the case in a subsequent trial (or disposition) on the merits of an antitrust damage suit. Respondent is just wrong. The court in *Kennedy* asserted that even an adverse decision with respect to *dismissal* or summary judgment (on a defense of immunity) does not preclude the "interposition of the defense of immunity as a defense to liability at the trial on the merits." *Id.*, 797 F.2d at 300. Thus, a court's earlier decision with respect to a motion for summary judgment or for dismissal is not the "law of the case" in a subsequent trial on the merits.

*Board of Trade of the City of Chicago v. Commodity Futures Trading Commission*, 605 F.2d 1016 (7th Cir. 1979), *cert. denied*, 466 U.S. 928 (1980), also supports Petitioner's position. That court stated that since a prior order reflected a discretionary ruling by the Court "*and not with respect to a plenary review of the merits* . . . ." it was not the law of the case in subsequent proceedings. *Id.*, 605 F.2d at 1020. Thus, a discretionary ruling by the trial court on an injunction does not become the law of the case in a subsequent trial (or Rule 12(b)(6) motion) on the merits.

*Angoon v. Hodel*, 803 F.2d 1016 (9th Cir. 1986), *cert. denied*, 484 U.S. 870 (1987), supports Petitioner's position. *Angoon* states the general rule that decisions on preliminary injunctions do not constitute the law of the case in a subsequent trial on the merits. Moreover, the *Angoon* court explained that it did not depart from this general rule, but rather considered the issues independently from its consideration of the same issues in the prior appeal, and simply came to the same conclusions.

Respondent claims that *Sierra Club v. U. S. Army Corps of Engineers*, 771 F.2d 409 (8th Cir. 1985), is inapposite to the case here. However, *Sierra Club* is important because it distinguishes the burden of proof required of a plaintiff in a preliminary injunction action from the legal standards which must be applied in a motion to dismiss (or a trial) on the merits. A decision - not on the merits - which disposes of a motion for a preliminary injunction is not the law of the case on a substantive issue on the merits. The courts below committed reversible error because they disregarded the critical differences between the tests applicable to an application for a preliminary injunction and the strict tests which must be satisfied before granting a Rule 12(b)(6) motion to dismiss. The rigorous standard of *Conley v. Gibson*, *supra*, in a Rule 12(b)(6) situation is far different from the element of "the likelihood of success on the merits" in a preliminary injunction matter.

3. **Respondent Bell has misrepresented the Record.**

It is axiomatic that review of a 12(b)(6) motion deals with the *legal sufficiency* of the Plaintiff's *pleading*, not with facts. Yet, Respondent purports to recite "facts" throughout its Brief in Opposition. Simply put, the facts are not at issue, only the *legal sufficiency* of Petitioner's Amended Complaint, to which Respondent did not file an answer.

One particularly offensive example is Respondent's allusion to the "parties have just concluded a three week evidentiary hearing before the Commission . . . ." (Respondent's Brief, p. 25). This comment is in violation of Supreme Court Rule 24, there being nothing in the Record to support this claim.

## CONCLUSION

At the heart of Respondent's argument is the wrong notion that state action immunity can apply to *any* activities or conduct directly or remotely related either to the rate tariffs of Respondent Bell or the *rate-making* functions of the state regulatory agency, the PUC. To support this erroneous idea, Respondent Bell made various claims in its trial brief on the injunction issue (R.23).

These bare assertions in a brief were relied upon by both courts below in disposing of the Plaintiff's lawsuit by claiming the Petitioner was challenging the ratemaking activities of Respondent Bell and the PUC. Of course, the Plaintiff's Amended Complaint (R.18; *See* particularly, R.18 at pp. 76-79 and paragraph 11 therein, together with the sworn affidavits, exhibits B and C attached to the original complaint (R.1)) alleges nothing of the kind. Rather, the Plaintiff's complaint alleges the private anticompetitive conduct of Defendant-Respondent Bell in threatening to cut off the telephone lines of a competitor who, as a customer of Bell, had paid his telephone bills every month. That is the "challenged conduct" which must be assessed in light of Respondent's trial brief claim that a state statute allegedly created immunity from the antitrust laws; not some other unpled conduct.

For the reasons stated in this Reply Brief, Petitioner respectfully prays that this Honorable Court issue its Writ of Certiorari to review the judgment of the United States Court of Appeals for the Fifth Circuit.

Respectfully submitted,

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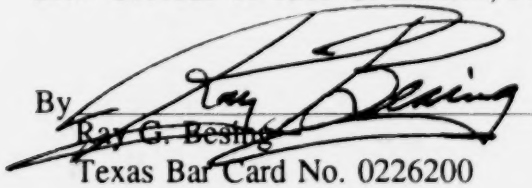
By 
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